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## **MEMORANDUM**

**DATE: March 3, 2005**

**TO: State Executives**

**FROM: Ron Raven, PMAA Excise Tax Counsel**  
**Holly Tuminello, Vice President**

**RE: Important news on Alcohol and Bio-diesel blend tax refund claims**

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On March 2, 2005, the IRS released the new form 8849, schedule 3 and its related instructions. This form is used for making claims on Alcohol and Bio-diesel fuel mixtures. The amount and nature of these claims was changed by the JOBS act effective January 1, 2005. Prior to 2005 there was no credit for bio-diesel blends and a series of reduced rates of tax due on alcohol blends. The JOBS act eliminated the reduced rate system and created a new refund system for both alcohol and bio-diesel blends.

Essentially the new system requires that the full rate of tax (\$.184 for gasoline-alcohol blends or \$.244 for bio-diesel blends) be paid into the highway trust fund for the entire quantity of the blended fuel. This tax is paid by the supplier on the gasoline or diesel portions of the blend when withdrawn from the terminal. The tax can also be paid by the supplier if the alcohol or bio-diesel is blended by him prior to the withdrawal from the terminal. In the event that the alcohol or bio-diesel is blended by someone other than the taxable fuel supplier or outside of the terminal, the blender owes the tax on the alcohol or bio-diesel added to the blend. The blender who had the tax liability for alcohol or bio-diesel added to the fuel is also entitled to a credit or refund for those gallons (\$.51 for alcohol, \$1.00 for agri-biodiesel or \$.50 for bio-diesel).

The critical question addressed in the forms is how the refund is to be realized. The answer is fairly simple for those persons who already had a tax liability due on their removals from the terminals: offset the liability with the credits. This is done (presumably since the new form 720 has not been released) by accruing

the liability for all gallons in the blend on part I of the 720, then reducing the schedule A liability by the credit amount claimed on schedule C and showing the net amount due in part III.

The more difficult procedure is for those blenders who had no liability for tax prior to the change in systems. Most of the alcohol blending had been done by marketers who had a 637T. They purchased the gasoline at a reduced rate, then purchased the alcohol at a tax-free price, made the blend and did not owe any tax. If they follow the same commercial pattern after January 1, 2005 the blenders will owe tax on the alcohol and have refund claims that are more than the tax due. The critical issue is the inter-relationship between the tax payment and the refund claim.

Schedule 3 of form 8849 (refund claim form) sets out following instruction:

*Before claiming a credit on Form 8849, the alcohol fuel mixture and bio-diesel mixture credit must be taken against any taxable fuel liability on Form 720. Any credit in excess of the section 4081 liability can be taken as a claim for payment on Form 8849 or an income tax credit on form 4136. You cannot claim any amounts on Form 8849 that you claimed (or will claim) on Schedule C (Form 720) or Form 4136.*

*Only one credit may be taken with respect to any gallon of alcohol reported on line 1 or bio-diesel reported on line 2. If any amount is claimed (or will be claimed) with respect to any gallon of alcohol on Form 720, or form 4136, then a claim cannot be made on Form 8849 for that gallon of alcohol or bio-diesel.*

For a blender who will have a refund claim in excess of his tax liability this appears to be the procedure:

For each deposit period of the quarter (1-15; 16-31 of each month) accrue the tax liability on the alcohol or bio-diesel at the taxable fuel rate into which it is blended (\$.184 for gasoline; \$.244 for diesel).

Fourteen days later, reduce the required deposit to \$0 by recognizing the reduction in net liability on schedule A of form 720 by applying the schedule C credits. This means you have effectively received a portion of the refund at that time.

Following the deposit date, apply for the excess credit on 8849 in dollars. The gallons will be different since you cannot apply 2 refunds on the same gallons, even at different rates.

For example, if a blender purchased 10,000 gallons of alcohol during the 1-15<sup>th</sup> of the month and blended it all into gasoline outside of the terminal during that period he would:

- a) Accrue a tax of \$1840 for 10,000 gallons on his form 720 part I liability;
- b) Reduce his deposit to \$0 on the 29<sup>th</sup> of the month (assuming no other taxable activity giving rise to a positive liability);
- c) Make a claim for \$3260 (\$5100 refund less \$1840 tax deposit reduction) for the period on form 8849, schedule 3 but not for 10,000 gallons of alcohol. Rather the claim will be for 6392 gallons to reflect that the other gallons had been received on the form 720;
- d) Continue this process 5 more times until the end of the quarter and then file the form 720 tax return showing \$0 net liability by showing 3608 gallons on schedule C.

As an alternative the blender could wait until the end of the quarter to make both the 720 and 8849 filing, but would give up the cash flow on the excess part of the refund (\$.326 on gasohol blends).

The same procedure is followed for bio-diesel blends except the credit rate may be either \$1.00 or \$.50 per gallon depending upon the producer certificate the blender received at time of purchase. In these cases the blender is seeking to recover an excess credit or either (\$.756 or \$.256 per gallon) but must still recalculate the gallons on schedule C of the 720 tax return and schedule 3 of the 8849 refund claim.

At this time there are no regulations reflecting these instructions on the form 8849. It is possible that the IRS will rescind or revise these procedures when regulations are released later this year.